BLANK PAGE

FILE COPY

Office - Supreme Court, U. S.
FILED
OCT 4 1940
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 50.

J. E. RILEY INVESTMENT COMPANY, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

BRIEF FOR PETITIONER.

ROBERT ASH,
Munsey Building,
Washington, D. C.,
Attorney for Petitioner.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

BLANK PAGE

INDEX

	Page
Opinions Below	1
Jurisdiction	1
Statutes Involved	1
Statement of the Case	2
Specification of Errors to be Urged	5
Summary of Argument	5
Argument	8
Statute says depletion shall be allowed	8
History of Percentage Depletion	9
Amended returns are recognized and have been uniformly construed as being amendments or supplements to the original return	11
Election is dependent upon the opportunity to choose between two or more conflicting courses and, in the absence of such an opportunity to choose, there can be no election	22
Point on which case decided not raised before Board of Tax Appeals or Circuit Court of Appeals	24

TABLE OF CASES

	Page
Bierce v. Hutchins, 205 U. S. 340	22
Connor v. United States, 19 F. Supp. 97	24
Dorothy Glenn Coal Mining Co., 38 B. T. A. 1154	5, 22
Fleischmann Company v. United States, 270 U. S. 349	17
General Utilities & Operating Company v. Helvering, 296 U. S. 200	25
Haggar Company v. Helvering, 308 U. S. 389	6, 7, 17, 18
Helvering v. Achelis, 112 F. (2d) 929	25
Helvering v. Clifford, 309 U. S. 331	25
Helvering v. Salvage, 297 U. S. 106	25
Helvering v. Tex-Penn Oil Company, 300 U. S. 481	25
Helvering v. Wood, 309 U. S. 344	25
Johnston, F. Harold, Executor, 33 B. T. A. 551	21
Lucas v. Sterling Oil & Gas Company, 62 F. (2d) 951	14, 23
McIntosh v. Wilkinson, 36 F. (2d) 807	20
Mead, C. H. Coal Company, 38 B. T. A. 1163	5
Mead, C. H. Coal Company, 106 F. (2d) 388	8, 15, 17, 18, 21
Morrow, Becker & Ewing, Inc. v. Commissioner, 57 F. (2d) 1	21
Pacific National Company v. Welch, 304 U. S. 191	20
Raymond, Ralph Leslie, 34 B. T. A. 1171	23
Rhodes v. Commissioner, 111 F. (2d) 53	25
Robertson, Callie E., 28 B. T. A. 635	23
Stewart v. Kahn, 11 Wall. (78 U. S.) 493	23
Texas Cement Company v. McCord, 233 U. S. 157	17
Union Metal Manufacturing Co., 1 B. T. A. 395	14
United States v. Merriam, 263 U. S. 179	23
Zellerbach Paper Co. v. Helvering, 293 U. S. 172	15

IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 50.

J. E. RILEY INVESTMENT COMPANY, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

BRIEF FOR PETITIONER.

Opinions Below.

The opinion of the Circuit Court of Appeals is reported at 110 F. (2d) 655, and appears in the record at pages 48-58. The memorandum findings of fact and opinion of the Board of Tax Appeals are not officially reported, but appear in the record at pages 19-28.

Jurisdiction.

Jurisdiction of this Court is conferred by Section 240 of the Judicial Code, as amended by the Act of February 13, 1925. The writ of certiorari was allowed by an order filed May 20, 1940. (R. 61)

Statutes Involved.

Sec. 23. Revenue Act of 1934:

"Deductions from Gross Income. In computing net income there shall be allowed as deductions: * * * (m)

Depletion—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion * * *, according to the peculiar conditions in each case: * * *"

Section 114 (b) (4), Revenue Act of 1934:

"Percentage Depletion for Coal and Metal Mines and Sulphur.—The allowance for depletion under section 23 (m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, 15 per centum, and, in the case of sulphur mines or deposits, 23 per centum, of the gross income from the property during the taxable year, * * *. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property. A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer * * *"

Statement of the Case.

The facts were fully found by the Board of Tax Appeals as follows: (R. 19-22)

"Petitioner is a corporation organized under the laws of Nevada, with its principal office and place of business at Flat, Alaska. Its business is the mining of gold.

"Flat is located in a remote part of Alaska on the 62nd parallel of latitude and 158th meridian of longitude. During the season of navigation, the usual means

of travel to Flat from Seward, the seaport, is from Seward, by railroad, to Nenana on the Yukon River, a distance of 415 miles, then by water via the Yukon River to Holy Cross, a distance of over 700 miles, and thence via a tributary of the Yukon to Flat, a distance of 420 miles. When navigation is not open, travel to and from Flat is either by plane or on foot. It requires about two weeks to go over the 400-mile trail on foot from Flat to Anchorage, which is the nearest town. The uncertainty and slowness of the winter mail service invariably resulted in current tax return forms reaching Flat too late for timely execution and filing. In order to avoid delinquency, it was the custom of petitioner's officers to use old return forms; consequently petitioner's original return for 1934 was filed on a 1933 form which had been mailed to petitioner by the Collector of Internal Revenue at Tacoma, Washington. In the winter of 1934, mail came to Flat part way by plane and part way by dog team. In order to be sure of filing the 1934 return on time, an officer of petitioner executed it on January 2, 1935, using the 1933 form, as stated. It reached Tacoma on January 29, but mail from Flat sometimes took two months in arriving at Tacoma.

"When petitioner's first 1934 return was filled out, its officers did not know of the statutory provisions allowing percentage depletion, but did know that unless the law had been changed, petitioner was not entitled to depletion, as it had no basis for cost depletion. The Collector, in sending the forms, had not advised the petitioner with respect to statutory depletion, and all the knowledge then available to it on this score was contained in Instruction No. 23 attached to the 1933 form, which reads as follows:

> '23. Depletion.—If a deduction is claimed on account of depletion, secure from the collector Form D (minerals), Form E (Coal) Form F (miscellaneous non-metals) Form O (oil and gas), or Form T (tim-

ber), fill in and file with return. If complete valuation data have been filed with Questionnaire in previous years, then file with this return information necessary to bring your depletion schedule up to date, setting forth in full statement of all transactions bearing on deductions or additions to value of physical assets with explanation of how depletion deduction for the taxable year has been determined. See Sections 23 (1) and 114 of the Revenue Act of 1932.'

"Petitioner's officer read the instructions before executing the return for 1934.

"Petitioner's officers first actually learned of the statutory depletion provisions in August, 1935, when a revenue agent visited Flat and advised that petitioner was entitled to percentage depletion for both 1933 and 1934. This agent prepared reports to that effect, as a result of which a refund was paid for 1933, but not for 1934; as to the latter year, the respondent ruled that petitioner had failed to claim percentage depletion in its original return and hence was not entitled to claim it subsequently.

"If petitioner's officers had known of the 1934 statutory provisions, they would have elected to take percentage depletion.

"As soon as petitioner's officers were advised that percentage depletion had been disallowed, they filed both an amended return claiming such depletion in the amount of $13,600.57, and a claim for refund.

"Petitioner's gross receipts from gold mining for the year 1934 were $99,711.56 and it has paid a tax for that year in the amount of $4,684."

In its opinion, the Board states (R. 25):

"Had petitioner's officers known of the election provided by the 1934 Act, they would have exercised it. Since petitioner had no basis for cost depletion, their 'election' in the premises, would really have been as between claiming a deduction and not claiming it, for

> if they did not deduct by a use of the percentage method, they could not deduct at all. Not knowing of this statutory right, their collective feeling at the time they executed the 1934 return was that they were not entitled to depletion of any kind."

The amended return filed by the petitioner was mailed February 8, 1936 and received by the Collector March 3, 1936. (R. 4, 8)

The Board of Tax Appeals, on the authority of *Dorothy Glenn Coal Mining Company,* 38 B. T. A. 1154, and *C. H. Mead Coal Company,* 38 B. T. A. 1163, affirmed the Commissioner on the ground that the "first return" designated in the statute meant the first form filed, so an election made in an amended return did not comply with the statute.

The Ninth Circuit affirmed the Board of Tax Appeals (Judge Mathews dissenting) (R. 48-58) and, in so doing, reached a conclusion in direct conflict with the Fourth Circuit in *C. H. Mead Coal Company* v. *Commissioner,* 106 F. (2d) 388.

Specification of Errors to be Urged.

1. The Court below erred in holding that the taxpayer is not entitled to depletion under Section 114 (b) (4) of the Revenue Act of 1934.

2. The Court below erred in holding that the claiming of percentage depletion in its amended return for 1934 did not comply with the provisions of Section 114 (b) (4) of the Revenue Act of 1934 and did not entitle the taxpayer to a deduction for percentage depletion.

3. The Court below erred in deciding for the Commissioner.

Summary of Argument.

The statute commands that a reasonable deduction for depletion *shall* be allowed. The section here involved merely states the method of computing the allowance. The "election" made in the "first" return to take or not to take percentage depletion governs all succeeding years. This tax-

payer, because of its isolated location in Alaska, had no knowledge of the provision for percentage depletion. Despite this, the Court below held that the doing of the impossible is a condition precedent for the deduction and, because the taxpayer failed to "elect", it must be perpetually punished for the failure.

All the revenue acts, beginning with that of 1913, have provided for a deduction for depletion. The administration of the section was difficult, and resulted in battles between experts to show basic valuations, depletable reserves and other facts. In 1926 percentage depletion was substituted for discovery depletion in the case of oil and gas wells "in the interest of simplicity and certainty of administration". A similar provision was made in 1932 in the case of coal, metal and sulphur mines. The 1934 Act continued the percentage depletion but stated that coal, metal and sulphur miners should state in their "first" return under the Act if they "elected" to take percentage depletion. Such an election governed all succeeding years.

Amended returns have always been recognized and have been uniformly construed as being amendments or supplements to the original return. Regulations, beginning with those under the 1916 Act, have provided for amended returns to correctly show items of income and deduction. So have Treasury rulings, Board of Tax Appeals and Court decisions, including decisions of this Court.

The rule is that a "first" return is a return for the first year. This includes not only the first form filed, but also an amended or completed return for the first year. A first return is no less a first return because amended.

The rule is in accordance with established law that pleadings and other documents may be amended to claim rights which existed when the original document was filed.

Haggar Company v. *Helvering*, 308 U. S. 389, is authority for this taxpayer's position. In prohibiting amendments to the declared value of capital stock, Congress legislated in the light of the established law permitting amended re-

turns. Had it intended the same prohibition to apply in the present case, it would have so provided in the statute. The 1934 Act contained the prohibition against amendment of the declared value in capital stock tax returns.

A timely amendment to a return is one made before the time for filing the return for the next succeeding year.

This case is not governed by the decisions which hold that a taxpayer, by an amended return, cannot change from one method of reporting income to a different method. In addition, in those cases, the taxpayer had the right to elect as to method.

Another line of cases which supports this taxpayer's position is that in which amended returns are permitted where the taxpayer has scant notice of radical changes in the law.

Election is dependent upon the opportunity to choose between two or more conflicting courses and, in the absence of such opportunity to choose, there can be no "election". The word has a judicially settled meaning and it is to be presumed that Congress legislated in the light of that meaning.

In interpreting the "election" provisions of Section 131 of the 1932 Act covering credits for foreign taxes paid, the Board and the Courts have had no difficulty in saying that the election can be made in an amended return. The failure to elect under section 131 results in denying the deduction for only one year and does not provide perpetual punishment, as does the rule of the Court below in the case at bar.

This case was decided below on the ground that the amended return was not timely. Before the Board and the Circuit Court of Appeals, the sole question presented was that an amended return was not a "first" return. This Court in the *Haggar* case decided that question favorably to the taxpayer. As the issue of timeliness was not raised below, it should not have been considered by the Circuit Court, and cannot be considered with propriety by this Court. Judge Mathews dissented on this ground in the Court below.

Argument.

Statute says depletion shall be allowed.

The Court is called upon to decide if, in computing income tax due from this taxpayer, it is entitled to a deduction for percentage depletion for 1934 and all subsequent years. The statute is specific in commanding that depletion *shall* be allowed to metal miners. The exact language is:

Sec. 23. Revenue Act of 1934:

> "In computing net income there *shall* be allowed as deductions: * * * (m) Depletion.—In the case of mines, oil and gas wells, other natural deposits and timber, a *reasonable allowance* for depletion * * * according to the peculiar conditions in each case * * *". (Italics supplied)

After providing that a reasonable deduction for depletion shall be allowed, Congress, in Section 114 (b) (4), merely prescribed the manner in which the allowance for depletion is to be computed. The purpose of Congress in providing percentage depletion was to broaden the allowance and remove administrative difficulties.[1] The decision below completely denies a deduction for depletion which the statute says shall be allowed, not only for 1934, but for all subsequent years, as the statute states that the election made in the "first" return shall be binding on all subsequent years.

In other words, although this taxpayer, because of its isolated location in the interior of Alaska, had no knowledge of the provision for percentage depletion and, therefore, could not "elect" to take the deduction, it is, under the

---

[1] The Fourth Circuit in *C. H. Mead Coal Company* v. *Commissioner*, 106 F. (2d) 388, states (P. 391): "We agree * * * that the depletion provisions of the Revenue Acts of 1932 and 1934 are liberalizing, rather than limiting, provisions and that Congress intended to allow depletion deductions by one of the two methods, and intended to give taxpayers a right to elect whichever method they preferred."

Circuit Court's decision, going to be perpetually punished. To put it another way, the Court below required the doing of the impossible as a condition precedent to the allowance of the deduction.

History of percentage depletion.

Beginning with the Act of October 3, 1913, the various Revenue Acts have provided for a deduction for depletion where income is derived from the extraction of natural deposits or timber.

The Revenue Act of 1918 (Sec. 234 (a) (9)), inserted language, which still remains in the statute, providing for the deduction: "In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion * * * according to the peculiar conditions in each case * * *". The 1918 Act also provided for "discovery" depletion where the fair market value of the property was grossly disproportionate to the cost.

The administration of the depletion sections, particularly the "discovery" depletion section, was difficult. In theory, the owner of a natural resource was supposed to own a certain number of depletable units, some of which were consumed each year, and he was allowed to deduct from income the cost or discovery valuation basis of the units consumed. In practice, great difficulties were encountered in determining basic valuations, depletable reserves, depletion rates and other facts.

In other words, the administration of the depletion section resolved itself into a battle between valuation and mining engineers and other experts representing the taxpayer on the one hand and the Commissioner on the other. In an effort to eliminate this confusion, Congress, in the 1926 Act, eliminated discovery depletion in the case of oil and gas wells and substituted percentage depletion. This step was taken "in the interest of simplicity and certainty in administration". (Seidman's Legislative History of Federal Income Tax Laws, p. 584)

The percentage depletion method worked so well in the case of oil and gas wells that percentage depletion was adopted and discovery depletion abandoned in the case of coal, metal and sulphur mines by Section 114 (b) (4) of the 1932 Act. The said Act did not require that a taxpayer make an election to take percentage depletion for 1933, but did require that he state in his 1933 return if he desired percentage depletion for all succeeding years, and that the depletion allowance should be computed for all succeeding taxable years in accordance with the election therein made.

The 1934 Act in Sec. 114 (b) (4) reenacted the percentage depletion provisions of the 1932 Act with reference to coal, metal and sulphur mines, but gave a new opportunity of election, stating:

> "A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, * * *."

The Senate and House Reports and the Congressional discussion all specifically state that the "election" provision was inserted "to avoid administrative complexity" (Seidman's Legislative History of Federal Income Tax Laws, page 353).

The "election" thus made would "avoid administrative complexity" in the case of those taxpayers using the percentage method by eliminating the battle of experts necessary to determine the essential facts used in computing

cost or discovery depletion. Or it might be that the purpose was the prevention of the taxpayers taking percentage depletion in one year, jumping to cost depletion the next, and vice versa.

Such switching apparently has not been a problem in the case of oil and gas producers, who may switch from one method in one year to another method in the next. Or they may use cost depletion for one "property" and percentage depletion for another "property" in the return for the same year.

In the case at bar, the Board states: (R. 25)

> "Had petitioner's officers known of the election provided by the 1934 Act, they would have exercised it. Since petitioner had no basis for cost depletion, their 'election' in the premises, would really have been as between claiming a deduction and not claiming it, for if they did not deduct by a use of the percentage method, they could not deduct at all."

Amended returns are recognized and have been uniformly construed as being amendments or supplements to the original return.

The deduction here sought was denied by the Commissioner on the sole ground that the taxpayer "failed to make an election in the original 1934 return". (R. 8) The amended return was treated as being of no effect. This brings us to a discussion of the practice of accepting amended returns and their effect.

In the case at bar the first return form for 1934, filed on a 1933 blank, reached the Collector at Tacoma, Washington, January 29, 1935. (R. 20) In August, 1935, a revenue agent visited Flat and advised the taxpayer it was entitled to percentage depletion for 1933 and 1934 and prepared reports to that effect. (R. 21) The Commissioner overruled the agent and held that, as the taxpayer had not claimed percentage depletion for 1934, it would not be allowed. As soon as petitioner's officers were advised that percentage

depletion had been disallowed, they mailed to the Collector an amended return claiming percentage depletion. (R. 22) The said claim was mailed February 8, 1936 and was received by the Collector March 3, 1936. (R. 4, 8)

There is no statutory provision for amended returns. However, such amended returns have always been recognized and accepted for the purpose of showing correct items of income and deduction. As long ago as Regulations 33, promulgated under the Act of September 8, 1916, as amended by the Act of October 3, 1917, it was stated in Article 128:

> "Amended Returns.—If, however, a corporation discovers or detects expenses or liabilities which were due or payable during a preceding year, it will be permissible for it to make an amended return for the year to which such expense or liability applies, include such expense in the deductions of that year, and file a claim for refund for any taxes overpaid by reason of the failure to deduct such expense or liability in the original return of that year."

The foregoing is important because it shows that, in the absence of statutory restriction on amending returns,[2] such amended returns have always been accepted to correctly reflect items of income and deductions.

Article 36 of Regulations 45 provide that taxpayers must file amended returns under certain circumstances where income has been overstated or understated.

Examples of other Regulations dealing with amended returns are:

> Regulations 45, Article 111 (1918 Act)
> Regulations 65, Articles 36, 112 (1924 Act)
> Regulations 69, Articles 36, 112 (1926 Act)

---

[2] For example, the capital stock tax provisions which were the basis of *Haggar Co.* v. *Helvering*, 308 U. S. 389.

Regulations 86 under the 1934 Act provided for amended returns in certain instances (Articles 43-2) and a similar provision has been carried through to Regulations 103 which are currently in effect. (Section 19. 43-2)

The Prentice-Hall Federal Tax Service, which is the standard reference work on Federal taxes, states: (¶17,089)

> "Although the law does not give specific rules regarding the filing of amended returns, this method of correcting errors made in returns of prior years has been consistently recognized. O. D. 113, C. B. 1919, p. 234, Mim. 2207 C. B. 1919, p. 221. O. D. 1131, C. B. Dec. 1921, p. 289. I. T. 1201, C. B. June, 1922, p. 345. I. T. 1450, C. B. June, 1922, p. 200, Reg. 103, Sec. 19, 43-2."

At ¶6009 B, the same Service states:

> "As in the case of amounts erroneously reported as income, the taxpayers' remedy (when items were erroneously claimed as deductions) is to file an amended return and a claim for refund. If the refund is barred, no other relief is available."

The rulings of the Treasury have been as consistent as the regulations on the question of amended returns.

Bulletin F, Bureau of Internal Revenue, states at page 33, (Prentice-Hall ¶14,260) that if a deduction for depreciation is, through inadvertence, not taken, an amended return showing the proper deduction, should be filed.

Where the funds of a minor were misappropriated by a guardian, it was held that amended returns, reflecting the facts, should be filed for 1917, 1918 and 1919. A. R. M. 144, C. B. Dec. 1921, p. 139.

T. D. 3220, C. B. Dec. 1921, p. 285 provided that all taxpayers who used appreciated or inflated value in determining the amount of their invested capital, must file amended returns within a designated time.

This brief will not be burdened with further citation of Treasury regulations or rulings to show the law is established that amended returns are acceptable to correct errors of income or deduction.

It is significant that in neither the regulations, nor the decisions, is there any requirement that amended returns, to be effective, must, as held in the Court below, be filed before the due date of the original return.

The Board of Tax Appeals also has, from the beginning, followed the same rule. In *Union Metal Manufacturing Co.*, 1 B. T. A. 395, the Board held that where a taxpayer failed to claim a deduction for the depreciation of patents in its original return, but did make such a claim in an amended return, the deduction should be allowed.

The Courts have had frequent opportunity to pass on the question of amended returns and have upheld the viewpoint of this taxpayer. In so doing, they have uniformly held that amended returns may be filed to show correct items of income and deduction. This is true even where the first return constituted an "election." In *Lucas* v. *Sterling Oil & Gas Co.*, 62 F. (2d) 951, 12 A. F. T. R. 90 the taxpayer under Treasury Regulations, had the option of charging certain expenditures in connection with oil and gas wells to capital or treating them as operating expense. An election, once made, was to control for all subsequent years. Taxpayer's original return for 1919 capitalized such expenditures. After other facts had been ascertained the taxpayer, February 10, 1921, filed an amended return which treated the expenditures as operating expenses. On neither return was a tax due. The 1920 return again treated such expenditures as operating expenses. Upon audit of the 1920 return the Commissioner ruled the expenditures for that year must be capitalized as the taxpayer had so elected in the 1919 return. The Court states (p. 951):

> "There is no statutory authority for amended returns, but it is well known that the Treasury Department, both in practice and by Regulation (Articles 36 and 111 of Regulations 45) has been liberal in authorizing and accepting such returns."

At page 952, the Court continues stating, that after learning that certain profits for 1919 should have been reported for that year, the taxpayer filed an amended return:

> "This seems to us to constitute the first instance of a mature and deliberate choice by the appellee, based upon knowledge of all the material facts * * * and, in view of the effect of an election upon future returns, we do not think that such election should be held to be effected, unless based upon knowledge of this kind as indicative of a final and deliberate choice. * * * and where the initial return is filed upon incomplete knowledge of the material facts, and before the filing of a return for the subsequent year, the taxpayer ascertains other pertinent facts and files an amended return disclosing them, it seems to us that the initial return may properly be regarded as tentative in its nature. and as not constituting an election. In such case, the taxpayer should be permitted to do what he had the right to do in the first instance."

To this day, amended returns showing correct items of income and deduction are accepted and are necessary in the orderly administration of taxing laws.

This Court has specifically passed on the effect of an amended return in *Zeilerbach Paper Co.* v. *Helvering,* 293 U. S. 172, which involved a question of limitation. Mr. Justice Cardozo states (p. 180):

> "From this administrative history, the inference is compelling that a second return, reporting an additional tax, is an amendment or supplement to a return already upon the files * * *."

The only possible conclusion to be reached from the foregoing is that an amended return must be considered in the same light as the original return. Consequently, in the case at bar, an "election" was made in the "first" return filed.

This is the construction adopted by the Fourth Circuit in *C. H. Mead Coal Co.* v. *Commissioner,* 106 F. (2d) 388, where it was stated: (p. 390)

> "In using the words 'first return' Congress evidently intended to include a completed first return, or a first return as properly amended and did not intend to limit

the taxpayer's right of election to the first form filed. Any other construction would, in fairness to the taxpayer, be too narrow and restricted. A first return is no less a first return because amended, provided the amendment be timely and is made to correct a mistake, made without any intent on the part of the taxpayer to take any undue advantage as to its tax payments, and without any bad faith. A different construction would, as said in the case of *Glenn* v. *Oertel Co.*, 97 Fed. (2d) 495, permit the government to lay a tax upon the taxpayer's errors rather than its income."

Later the Court states:

"* * * we are forced to the conclusion that in all fairnes, and certainly fairness is to be expected from a government in dealing with its taxpayers, the amendment to the return should have been allowed. In rejecting the amendment, the Commissioner was in error."

Still later in the opinion the Court states:

"If an amendment made to correct a mistake, presented within a reasonable time, is rejected through a narrow and harsh construction of the law, to the detriment of the taxpayer, such rejection is arbitrary and unjust. It certainly is not the duty of the Commissioner to deprive a taxpayer of any rights justly due him."

The Court goes further and says:

"We agree with the contention made on behalf of the petitioner that the depletion provisions of the Revenue Acts of 1932 and 1934 are liberalizing, rather than limiting, provisions and that Congress intended to allow depletion deductions by one of the two methods, and intended to give taxpayers a right to elect whichever method they preferred. The decision of the Board in this case deprives the petitioner of that right."

The *Mead* case involved the same statute as the case at bar. The facts in the *Mead* case are that the taxpayer,

when filing its return for 1933, did not claim depletion because it had a loss. However, it attached a statement to its return stating it elected to take percentage depletion for all subsequent years in the case of certain listed properties. In its return for 1934 the taxpayer, acting on the erroneous advice of counsel, did not take depletion. Some time later, as the result of a conversation with a Revenue Agent, the taxpayer decided it had the right to take such depletion. Accordingly, on February 6, 1936, it filed an amended return and claim for refund. The Commissioner disallowed the depletion deduction on the ground the taxpayer had not "elected" to take it in its first return filed under Section 114 (b) (4) of the Revenue Act of 1934. The Board of Tax Appeals sustained the Commissioner. 38 B. T. A. 1163.

The rule, as stated in the cases just mentioned, is in conformity with the established law of construction.

> "It is elementary that an amendment dates back to the filing of the petition and is to supply defects then existing, or at most to bring into the suit grounds of action which existed at the beginning of the case." *Texas Cement Co.* v. *McCord,* 233 U. S. 157, 164.

In the case at bar, the taxpayer merely claimed in the amended return, a deduction to which it was entitled when the first form was filed. It must be remembered that, as stated in the *Mead Coal Company* case, "Congress intended to allow depletion deductions by one of the two methods."

> "The strict letter of an act must, however, yield to its evident spirit and purpose, when this is necessary to give effect to the intent of Congress." *Fleischmann Co.* v. *United States,* 270 U. S. 349, 360.

The Court below relied heavily on *Haggar Co.* v. *Helvering,* 308 U. S. 389. Obviously, that case does not control here, and in reality bears out this taxpayers' contention.

The *Haggar* case involved Sections 215 and 216 of the National Industrial Recovery Act, which imposed a capital stock tax and an excess profits tax based on the value of the

capital stock stated in the "first return" filed under the Act. The statute specifically provided that the capital stock tax value as declared in the return could not be amended. The language of the statute, including the prohibition of amendment of the declared value, was re-enacted into the Revenue Act of 1934, which is the statute involved in the case of bar.

The only logical explanation of the prohibition against amendment of the declared value is that Congress legislated in the light of the established and well known practice of accepting amended returns. If the law had been established to the effect that amended returns were not permissible, the specific prohibition would have been unnecessary. Also, if Congress had intended to prohibit amendments to returns under the section involved in the case at bar, it would have so provided, as it did in the section of the same 1934 statute covering capital stock tax returns.

It should be remembered that in the *Haggar* case, this Court permitted an amendment of the value declared in the first form filed, although the statute specifically provided that the value declared in the "first return" could not be amended. It is true that the amended return was filed within the time permitted for the filing of returns. This Court held, however, the "first return" meant the return for the first year and cited *C. H. Mead Coal Company,* 106 F (2d) 388, as authority for that holding.

This taxpayer contends that the rule of the *Mead* case is the logical rule under the section of the statute here involved, *i. e.,* a "first return" is a "completed first return, or a first return as properly amended," and a taxpayer's right of election is not limited to the first form filed. "A first return is no less a first return because amended, provided the amendment be timely and is made to correct a mistake." The Court held that a "timely" amendment was one made before the time for filing the return for the next succeeding year. It further held that if an amendment made to correct a mistake was filed within a reasonable time and was re-

jected, its rejection was a harsh, arbitrary and unjust construction of the law.[3]

By inference, at least, this Court approved this conclusion by citing the *Mead* case in the Haggar decision.

As pointed out on page 12 Regulations, beginning with Regulations 33 under the 1916 and 1917 Acts, provided for amended returns to correctly show expenses or liabilities for prior years. Such amended returns could be filed any time prior to the expiration of the limitation covering refunds. By practice and regulation continuing to the present time, such amended returns are permissible. In fact, it would be difficult to correct errors if they were not permitted. The Court below States (R. 54): "Art. 43-2 of Regulations 86 (1934 Act) which permits the filing of an amended return for the purpose of deducting a loss occurring during a prior taxable year, but not then ascertained, indicates that such a return may be filed at any time within the period allowed for claiming a refund."

It may very well be, however, that, as the percentage depletion provision was inserted in the law "to avoid administrative complexity," the proper rule when dealing with that section is to limit amended returns to those filed before the return is due for the following year. Such a return was held to be "timely" in the *Mead Coal Company* case. By thus "electing" in the "first return," even if by an amended or completed first return, administrative complexity would be eliminated. The completed return for the first year would thus govern all succeeding years. Actually, however, the taking of cost depletion one year, percentage depletion the next, and vice versa, does not cause any administrative problems in the case of oil and gas wells, where such procedure is permissible, and where nearly all taxpayers use the percentage method. Possibly the more logical explanation of the purpose of avoiding "admini-

[3] The amended return in the *Mead* case was filed February 6, 1936. In the case at bar, the amended return was mailed February 8, 1936, but due to taxpayer's isolated location was not received by the Collector until March 3, 1936.

strative complexity'' was that an election to take percentage depletion would eliminate the battle of experts necessary to determine the essential facts used in computing cost or discovery depletion.

The Court below cites *Pacific National Company* v. *Welch*, 304 U. S. 191, as authority for denying effect to the amended return. The case is typical of a line of cases, some of which are cited in the footnote to the decision below (R. 55) to the effect that a taxpayer who elects to report income by one method cannot later change to an entirely different method.

Illustrations of such situations are when a taxpayer reports on a cash basis and attempts to file an amended return on the accrual basis; a husband and wife file a joint return and later attempt to file separate returns; or, where affiliated corporations file consolidated or separate returns and, later, attempt to change the method.

It is important to note that in the *Pacific National* case, and all other cases of this type, the taxpayer actually had the opportunity of election of one method of reporting income as compared with another. In the case at bar, there was no real election for, as the Board states, (R. 25), ''their 'election' * * * would really have been as between claiming a deduction and not claiming it, for if they did not deduct by use of the percentage method, they could not deduct at all. Not knowing of his (this) statutory right, their collective feeling at the time they executed the 1934 return was that they were not entitled to depletion of any kind.''

In the type of cases mentioned above, the law unquestionably prohibits amended returns, although there are some exceptions, where the facts are unusual.[4] The case at bar, however, does not involve a change of *method*, but deals entirely with an item of deduction which is permitted under the decisions previously mentioned herein.

The *Pacific National* case involved a situation where the taxpayer reported the sale of lots as completed transactions in 1928. In 1931, it filed an amended return of a different

---

[4] See *McIntosh* v. *Wilkinson*, 36 F. (2d) 807.

kind, which computed the gain on the entirely different installment method. This Court held such a change of *method* was improper, stating (p. 194):

> "Change from one *method* to the other, as petitioner seeks, would require recomputation and readjustment of tax liability for subsequent years and impose burdensome uncertainties upon the administration of the revenue laws * * *. There is nothing to suggest that Congress intended to permit a taxpayer, after expiration of the time within which return is to be made, to have his tax liability computed and settled according to some other *method.*" (Italics supplied)

Another line of cases holds that it is a breach of discretion for the Commissioner to refuse to accept amended returns in cases where the taxpayer has scant notice of radical changes in the law. The leading case is *Morrow, Becker & Ewing, Inc.* v. *Commissioner,* 57 F. (2d) 1, which is cited with favor in the *Mead Coal Company* case and wherein the Fifth Circuit states: (P. 3)

> "In views of the radical changes in the law, of which the petitioner had scant notice, if any, in fairness and justice to the taxpayer the returns should have been received and considered. Taxes are assessed on income and not on honest mistakes of the taxpayer. It was the duty of the Commissioner to do nothing arbitrary or unreasonable that would deprive petitioner of rights created by the new law and the regulations thereunder. It was a breach of discretion on the part of the Commisioner not to receive the amended return form for 1925 under the circumstances disclosed."

See also *F. Harold Johnston, Executor,* 33 B. T. A. 551.

In the case at bar, the regulations interpreting the 1934 Act were not released to the public until March 2, 1935, so this taxpayer, because of its isolated position, could not have secured a copy of the regulations prior to March 15, let alone in time to file a return prior to that date.

Election is dependent upon the opportunity to choose between two or more conflicting courses and, in the absence of such opportunity to choose, there can be no election.

The statute specifically states the taxpayer shall "state whether he elects" to have depletion computed on the percentage basis. The Board points out: (R. 25)

> "Had petitioner's officers known of the election provided by the 1934 Act, they would have exercised it. Since petitioner had no basis for cost depletion, their 'election' in the premises, would really have been as between claiming a deduction and not claiming it, for if they did not deduct by a use of the percentage method, they could not deduct at all. Not knowing of his statutory right, their collective feeling at the time they executed the 1934 return was that they were not entitled to depletion of any kind."

This Court will judicially notice that Regulations 86, promulgated under the 1934 Act, were not approved by the Secretary of the Treasury until February 11, 1935. After approval, the regulations were printed and were not released to the public until March 2, 1935, so could not have reached the taxpayer prior to the time for filing the "first" return. (See official print of regulations and Report No. 13, Prentice-Hall 1935 Federal Tax Service, dated March 7, 1935)

It is fundamental that no person can be held to have made an "election" unless advised of the two or more opportunities open to him and he selects one. The rule is stated by Mr. Justice Holmes in *Bierce* v. *Hutchins*, 205 U. S. 340, 346, as:

> "Election is simply what its name imports; a choice, shown by an overt act, between two inconsistent rights, either of which may be asserted at the will of the chooser alone."

Chairman Arundell of the Board of Tax Appeals in his dissenting opinion in *Dorothy Glenn Coal Co.*, 38 B. T. A.,

1154, which involved a construction of the same statute here involved, states: (p. 1162)

> "Election presupposes the existence of the right of a choice between alternatives. *Allis* v. *Hall*, 56 Atl. 637; *Standard Oil Co.* v. *Hawkins*, 74 Fed. 395; *McIntosh* v. *Wilkinson*, 36 F. (2d) 807; *Tide Water Oil Co.*, 29 B. T. A. 1208; 48 Harvard Law Review 1281. To say that one is put to his election when he has no choice is to give him nothing more than a 'Hobson's choice.' The Acts of 1932 and 1934 both use the terms 'elects' and 'election.' These words become meaningless if applied so as to require an election where there is no right of choice."

Lucas v. *Sterling Oil & Gas Co.*, 62 F. (2d) 951, (C. C. A. 6) previously quoted herein at page 14 is likewise authority on the question of "election." To the same effect see *Callie E. Robertson*, 28 B. T. A. 635, 639.

The foregoing clearly shows that "elect" has a judicially settled meaning. Consequently, it must be presumed it was used in that sense by Congress. In *U. S.* v. *Merriam*, 263 U. S. 179, 4 A. F. T. R. 3673, the Supreme Court states: (p 187)

> "The word * * * having the judicially settled meaning which we have stated, we must presume it was used in that sense by Congress." (Citing authorities)

In addition, the provision here involved is remedial. The rule of construction is:

> "The statute is a remedial one and should be construed liberally to carry out the wise and salutary purposes of its enactment." *Stewart* v. *Kahn*, 11 Wall. (78 U. S.) 493, 504.

In addition to the cases previously referred to, the Courts and the Board have had no difficulty with questions similar to the one here involved.

Ralph Leslie Raymond, 34 B. T. A. 117., (acquiesced in by the Commissioner In G. C. M. 19727), C. B. 1938-1,

p. 255, involved an interpretation of Sec. 131 of the 1932 Act, which provides that taxpayers will be allowed credit for foreign taxes paid "if the taxpayer specifies on his return his desire to have the benefits of this section". In that case the taxpayer filed a non-taxable return and did not claim credit for Canadian taxes paid. Upon audit, a loss was disallowed and the Commissioner disallowed the credit under Sec. 131, because the taxpayer had failed to signify on his return that he desired the benefits of this section. The Board in its opinion reviewed the cases on election and properly holds that the taxpayer should prevail.

A similar result was reached in *Connor* v. *U. S.*, 19 F. Supp. 97, 19 A. F. T. R. 683, wherein the Court, construing the foreign tax paid credit section, held "the law should not be interpreted to require the impossible", stating, "the petitioner was not called upon to make any election under Section 131 (a) as the word 'election' signifies a choice between two or more methods."

It should be observed that in the section 131 cases just cited, the taxpayer was, under the Commissioner's rulings, penalized only to the extent of being denied the claimed deduction for one year. Upon appeal, the Commissioner was reversed. In the case at bar, the taxpayer is, under the Circuit Court opinion, going to be perpetually punished by being denied any depletion deduction for all subsequent years.

Point on which case decided not raised before Board of Tax Appeals or Circuit Court of Appeals.

In the Court below, Judge Mathews dissented (R. 58), on the ground that, before the Board of Tax Appeals, the Commissioner made the sole contention that the amended return was not a "first return." Judge Mathews was of the opinion that the said contention should be rejected on the authority of the *Haggar* case. He further said that, as the question of the timeliness of the amended return was

not raised before the Board or the Circuit Court, the Court could not, with propriety, consider or decide any such question.

The dissenting opinion states the law. This Court states in *Helvering* v. *Tex-Penn. Oil Co.*, 300 U. S. 481, 498, as follows:

> "He sought no ruling upon the question from the Board or the lower court and is, therefore, not entitled to have it decided here."

As recently as *Helvering* v. *Wood*, 309 U. S. 344, decided February 26, 1940, and *Helvering* v. *Clifford*, 309 U. S. 331 (April 22, 1940) the same rule was invoked. See also:

General Utilities and Operating Co. v. *Helvering*, 296 U. S. 200.
Helvering v. *Salvage*, 297 U. S. 106.
Rhodes v. *Commissioner*, (C. C. A. 4) 111 F. (2d) 53.
Helvering v. *Achelis*, (C. C. A. 2) 112 F. (2d) 929.

Under the above mentioned authorities this Court cannot, with propriety, consider the question of the timeliness of the amended return.

Respectfully submitted,

ROBERT ASH,
Munsey Building,
Washington, D. C.,
Attorney for Petitioner.

October, 1940.